



The following constitutes the Memorandum Decision of  
the Court. Signed: December 9, 2022

A handwritten signature in black ink, reading "Roger L. Efremsky", is positioned above the judge's name.

Roger L. Efremsky  
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF CALIFORNIA  
OAKLAND DIVISION

In re

PACIFIC STEEL CASTING COMPANY LLC,                      Case No. 19-40193 RLE  
Debtor.    Chapter 7

SARAH L. LITTLE, Ch. 7 Trustee,  
Plaintiff,    AP No. 19-4057 RLE

v.

SPEYSIDE FUND, LLC, et al.,  
Defendants.

**Memorandum Decision on Motion for Summary Judgment**

**I. Background**

In January 2019, Pacific Steel Casting Company, LLC  
("Pacific Steel" or "Debtor") filed this chapter 7 case and Sarah  
L. Little was appointed trustee (the "Trustee"). In November

1 2019, the Trustee commenced this adversary proceeding.

2 The First Amended Complaint (the "FAC") alleged that  
3 Debtor's managers (the "Speyside Managers") breached the  
4 fiduciary duties they owed to the Debtor and its stakeholders,  
5 and Debtor's members aided and abetted them in this (the  
6 "Speyside Members" and, collectively with the Speyside Managers,  
7 the "Speyside Defendants"). Docket No. 70 (second claim and  
8 fourteenth claims for relief).

9 The FAC also alleged that Debtor's outside auditor,  
10 defendant UHY, LLP ("UHY") aided and abetted the breach of  
11 fiduciary duty committed by the Speyside Managers. Docket No. 70  
12 (third claim for relief).<sup>1</sup>

13 UHY responded to the FAC, generally denying its allegations  
14 and stating the Trustee had "unclean hands" as an affirmative  
15 defense. Docket No. 72 (third affirmative defense). After  
16 completing discovery, UHY moved for summary judgment, the Trustee  
17 filed opposition and the matter was then taken under submission.  
18 Docket Nos. 148-150, 158-159, 164-165.

19 Thereafter, the Speyside Defendants and the Trustee filed  
20 their motions for summary judgment as to the fact of liability.  
21 Docket Nos. 171-174, 203, 205 and 176, 180-183, 195, 199, 208.

22 On August 17, 2022, the court issued its Memorandum Decision  
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24 <sup>1</sup> See FAC ¶12-13 (Defendants violated their fiduciary duties,  
25 UHY aided and abetted this); ¶123 (listing alleged breaches of  
26 fiduciary duty); ¶127 (UHY provided material assistance by  
27 providing materially false financial statements, which  
perpetuated the wholesale failure to account for known  
liabilities and the unsubstantiated inflation of assets).

1 granting the Speyside Defendants' motion for summary judgment and  
2 denying the Trustee's motion for summary judgment as to the fact  
3 of liability. Docket No. 231. The Memorandum Decision is  
4 incorporated herein by reference. The court ruled, *inter alia*,  
5 that the Speyside Defendants were entitled to summary judgment in  
6 their favor and the court would dismiss the Trustee's breach of  
7 fiduciary duty and aiding and abetting claims against the  
8 Speyside Defendants. The court also held that the aiding and  
9 abetting breach of fiduciary claim against UHY was necessarily  
10 moot and would also be dismissed. The court then entered its  
11 order granting summary judgment in UHY's favor. Docket No. 235.

12 The Memorandum Decision did not address any of the  
13 substantive arguments UHY had made in its motion for summary  
14 judgment or the counter-arguments made by the Trustee. UHY has  
15 since suggested the Court should rule on the merits of UHY's  
16 motion. Docket No. 270. The Trustee concurred.

17 The court will now expand on its ruling in UHY's favor. The  
18 court assumes the parties are familiar with the relevant factual  
19 and legal background in this case and it will not be described in  
20 any detail.

## 21 **II. Summary Judgment Arguments**

### 22 **A. UHY's Motion**

23 UHY's first argument is that it is entitled to summary  
24 judgment because, under California law, the defense of *in pari*  
25 *delicto* - or unclean hands - bars the Trustee's claim against it.

26 The doctrine of *in pari delicto* dictates that when a  
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1 participant in illegal, fraudulent, or inequitable conduct seeks  
2 to recover from another participant in that conduct, the parties  
3 are deemed *in pari delicto*, and the law will aid neither of them.  
4 *In re Mortgage Fund'08 LLC*, 527 B.R. 351, 366 (N.D. Cal. 2015);  
5 *In re Yellow Cab Cooperative, Inc.*, 602 B.R. 357, 360-62 (Bankr.  
6 N.D. Cal. 2019). Under this theory, the Trustee is deemed to be a  
7 participant in the alleged wrongdoing of the Speyside Defendants.

8 UHY's second argument is that it is entitled to summary  
9 judgment because it has shown that there is an absence of  
10 evidence to support the Trustee's aiding and abetting claim.  
11 *Celotex Corp. v. Catrett*, 477 U.S. 317, 324 (1986). UHY contends  
12 that (1) the Trustee has not raised a triable issue of fact that  
13 UHY had actual knowledge of the specific wrongdoing she has  
14 alleged - that the Speyside Defendants "looted" the Debtor; and  
15 (2) the Trustee has not raised a triable issue of fact that UHY  
16 knowingly gave substantial assistance to the Speyside Defendants  
17 in doing this "looting." UHY argues that, at most, the Trustee's  
18 case is one of professional malpractice because her case against  
19 UHY relies on alleged inadequate auditing of the Debtor's  
20 financial statements.

#### 21 **B. The Trustee's Opposition**

22 In her opposition, the Trustee argues that the Debtor is a  
23 Delaware limited liability company and the breach of fiduciary  
24 duty and aiding and abetting claims implicate the internal  
25 affairs doctrine which means that Delaware law applies. Under  
26 Delaware law, the *in pari delicto* defense is not available to  
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1 fiduciaries and is not available to a non-fiduciary such as UHY.  
2 *Stewart v. Wilmington Trust SP Services, Inc.*, 112 A.3d 271  
3 (Del.Ch.2015), *aff'd* 126 A.3d 1115 (Del. Nov. 2, 2015) (declining  
4 to dismiss aiding and abetting claim against outside auditor  
5 because Delaware's fiduciary duty exception to *in pari delicto*  
6 covered this claim). In addition, the Trustee claims Delaware's  
7 interest in having its law applied is paramount to California's  
8 interest in having its law applied. *American International Group,*  
9 *Inc.*, 965 A.2d 763, 822 (Del.Ch.2009) (professional malpractice  
10 and breach of contract claims against auditor did not implicate  
11 internal affairs doctrine; following *Restatement* approach, court  
12 found New York had the most significant relationship to the  
13 claims and New York's *in pari delicto* defense immunized auditor  
14 from these claims; court noted it would reach a different result  
15 if plaintiffs stated aiding and abetting breach of fiduciary duty  
16 claim because Delaware's policy interest would then be  
17 paramount). The Trustee faults UHY for not performing a choice of  
18 law analysis, and for not recognizing that the internal affairs  
19 doctrine governs the outcome here.

20 The Trustee also claims she has established there is ample  
21 evidence that UHY knowingly aided and abetted the Speyside  
22 Managers' breaches of fiduciary duty.

23 **C. UHY's Reply**

24 In its reply, UHY points out that the Trustee previously  
25 argued - and convinced the Court to hold - that her fraudulent  
26 transfer claims against the Speyside Defendants were tort claims  
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1 to which California law applied because California had the most  
2 significant relationship to these claims.<sup>2</sup> UHY contends this is  
3 now the law of the case and principles of judicial estoppel  
4 preclude the Trustee's belated switch to Delaware law.  
5 *Mayweathers v. Terhune*, 136 F.Supp.2d 1152, 1153-54 (E.D. Cal.  
6 2001) (citing *Arizona v. California*, 460 U.S. 605 (1983), under  
7 law of the case doctrine, when a court decides on a rule it will  
8 ordinarily follow it during the case); *New Hampshire v. Maine*,  
9 532 U.S. 742, 750-51 (2001) (explaining judicial estoppel).<sup>3</sup>

10 UHY also points out that in her verified responses to UHY's  
11 interrogatories, the Trustee took the position that California  
12 law applied to her aiding and abetting claim. The Trustee stated:

13 Under **California law**, aiding and abetting requires Plaintiff  
14 to prove the following three elements: (1) that UHY knew  
15 that a breach of fiduciary duty was being committed by the  
16 owners of the Debtor; (2) that UHY gave substantial  
17 assistance or encouragement to the owners of the Debtor; and  
18 (3) that UHY's conduct was a substantial factor in causing  
19 harm to Plaintiff. CACI 3610; see also *Casella v. SouthWest  
20 Dealer Services, Inc.*, 157 Cal. App.4th 1127, 1140-41  
21 (2007).

22 Docket No. 165, Quadrozzi Dec., Ex. 21, 4:10-19 (emphasis added).  
23 The Trustee also stated:

24 The damages for aiding and abetting a breach of fiduciary  
25 duty, especially one where, as here, that aiding and  
26 abetting began at the inception of the alleged looting by  
27 the owners of the Debtor, under **California law** is  
28 coextensive with the damages sought by plaintiff against the  
owners.

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24 <sup>2</sup> See *Restatement (Second) of Conflict of Laws* §145 listing  
25 factors to analyze for tort claims.

26 <sup>3</sup> UHY also points out that the same facts support the  
27 Trustee's fraudulent transfer, breach of fiduciary duty, and  
aiding and abetting claims. Docket No. 164, 10:8-25.

1 Docket No. 165, Quadrozzi Dec., Ex. 21, 3:11-13 (emphasis added).

2 Based on this history, UHY argues that under principles of  
3 judicial estoppel and the law of the case doctrine the Trustee  
4 may not now claim that Delaware law applies.

### 5 **III. Discussion**

#### 6 **A. Standard for Summary Judgment**

7 Summary judgment is proper when the moving party shows that  
8 there is no genuine dispute as to any material fact and the  
9 moving party is entitled to judgment as a matter of law.  
10 Fed.R.Civ.P. 56(a), applicable here by Bankruptcy Rule 7056. The  
11 purpose of summary judgment "is to isolate and dispose of  
12 factually unsupported claims or defenses." *Celotex Corp. v.*  
13 *Catrett*, 477 U.S. 317, 323-24 (1986).

14 The moving party has the initial responsibility of informing  
15 the court of the basis for its motion, and identifying the  
16 evidence which it believes demonstrates the absence of a genuine  
17 issue of material fact. *Id.* If the moving party meets its initial  
18 burden, the burden shifts to the nonmoving party to establish,  
19 beyond the pleadings, that there is a genuine issue for trial.  
20 *Id.* at 324. Where a rational trier of fact could not find for the  
21 non-moving party based on the record as a whole, there is no  
22 genuine issue for trial. *Matsushita Elec. Indus. Co. v. Zenith*  
23 *Radio Corp.*, 475 U.S. 574, 587 (1986).

#### 24 **B. Choice of Law**

##### 25 **1. Estoppel theories**

26 UHY argues that the Trustee should be judicially estopped  
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1 from taking the position that Delaware law applies because (1)  
2 the Trustee took the position that California law applied to tort  
3 claims such as her fraudulent transfer claims against the  
4 Speyside Defendants and these claims are premised on the same  
5 facts alleged in her claim against UHY; (2) the court adopted  
6 this position in ruling in her favor on the Speyside Defendants'  
7 motion to dismiss; (3) it would be unfair to allow the Trustee to  
8 depart from this position now. *New Hampshire v. Maine*, 532 U.S.  
9 742, 750-51 (2001).

10 Because the fraudulent transfer claims and the aiding and  
11 abetting claim are premised on the same facts and the Trustee  
12 took the position - and the court agreed - that the fraudulent  
13 transfer claims were torts to which California law applied  
14 because it had the most significant relationship to them, the  
15 elements for judicial estoppel are satisfied. At this late stage  
16 of the litigation, the court will not allow the Trustee to depart  
17 from her earlier position on which she succeeded in defeating the  
18 Speyside Defendants' motion to dismiss.

19 UHY also argues that this previous ruling means use of  
20 California law for tort claims is now the law of the case. The  
21 court's previous ruling regarding choice of law pertained to the  
22 identical issue now before the court in the sense that the court  
23 ruled that California law applied to tort claims.

24 UHY also urges the Court to apply California law to the  
25 aiding and abetting claim because the Trustee stated under oath  
26 in her Interrogatory Responses that it did. This is a compelling  
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1 argument. There is obvious unfairness in allowing the Trustee to  
2 disclaim her choice of law at this late stage of the litigation.<sup>4</sup>

3 The Trustee based her case against UHY on California law  
4 until she filed her opposition to UHY's motion. UHY asserted  
5 unclean hands as an affirmative defense in its Answer. The  
6 Trustee relied on California law in responding to UHY's discovery  
7 and broadly took the position that California law applied to tort  
8 claims. If the Trustee intended to rely on Delaware law, this  
9 should have been made clear long ago. The position she has taken  
10 cannot now be casually discarded. Accordingly, under principles  
11 of estoppel and the law of the case doctrine, California law  
12 applies.

## 13 **2. Internal Affairs Doctrine**

14 The Trustee claims that because Debtor is organized under  
15 Delaware law, the internal affairs doctrine means that Delaware  
16 law applies to the breach of fiduciary duty claim against the  
17 Speyside Managers and also to the aiding and abetting claim  
18 against UHY. UHY counters that the aiding and abetting claim  
19 against it does not concern the Debtor's internal affairs, UHY  
20 was not a fiduciary to the Debtor, and there is no reason to  
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23 <sup>4</sup>The Trustee argued California law applied to tort claims in  
24 April 2020. The FAC and UHY's Answer to it were filed in June  
25 2020. The responses to UHY's interrogatories were signed in July  
26 2021. Fact discovery closed in July 2021 by stipulation of the  
27 parties. The Trustee did not raise this choice of law point until  
March 2022. The Trustee also relied on California law in her  
response to a Speyside Defendant's interrogatories. On these  
facts, the argument for using Delaware law was not timely raised  
and appears to be an afterthought.

1 apply Delaware law when California has a more significant  
2 relationship to the underlying events.

3 The internal affairs doctrine is a conflict of laws  
4 principle which recognizes that only one state should have the  
5 authority to regulate a corporation's internal affairs. *Lidow v.*  
6 *Superior Ct.*, 206 Cal.App.4th 351, 358-59 (2012). Internal  
7 affairs are generally understood to mean matters peculiar to the  
8 relationships among or between the corporation and its current  
9 officers, directors, and shareholders – because otherwise a  
10 corporation could be faced with conflicting demands. *Id.*

11 In determining whether the internal affairs doctrine applies  
12 here, the court finds instructive *In re Brocade Commc'ns Sys.,*  
13 *Inc. Derivative Litig.*, 615 F.Supp.2d 1018, 1036 (N.D. Cal.  
14 2009). There, the parties disputed whether Delaware (the state of  
15 incorporation) or California law should apply to tort claims  
16 brought against non-fiduciaries. After noting that the doctrine  
17 generally means that the law of the state of incorporation  
18 governs causes of action that implicate a company's internal  
19 affairs, the court declined to apply Delaware law to tort claims  
20 brought against individuals who were not fiduciaries and applied  
21 California law instead. *See also Solow v. Stone*, 994 F.Supp. 173,  
22 177 (S.D.N.Y.1998) (declining to apply internal affairs doctrine  
23 to aiding and abetting breach of fiduciary claim but  
24 acknowledging it applied to breach of fiduciary claim against  
25 officers); *In re Heritage Organization, L.L.C.*, 413 B.R. 438, 463  
26 (Bankr. N.D. Tex. 2009) (collecting cases involving whether

1 internal affairs doctrine applied to a trustee's fraudulent  
2 transfer claims; ruling Texas's internal affairs doctrine,  
3 dictating use of formation state's law, did not apply to  
4 trustee's fraudulent transfer claims because such claims involve  
5 the rights of creditors not internal corporate governance  
6 issues).

7       Based on the undisputed facts in this record showing that  
8 UHY was not a fiduciary to the Debtor and merely an outside  
9 auditor, the court finds the internal affairs doctrine is not  
10 implicated here and does not determine the outcome of the choice  
11 of law question.

### 12           **3. Governmental Interest Analysis**

13       The Trustee's alternative argument is that, if the internal  
14 affairs doctrine does not apply, Delaware has a paramount  
15 interest in having its law applied. Under Delaware law, the *in*  
16 *pari delicto* defense would not be available for UHY according to  
17 the Trustee. *Stewart v. Wilmington Trust SP Services, Inc.*, 112  
18 A.3d at 318-20 (*in pari delicto* defense is not available to  
19 fiduciaries, court extends this rule to non-fiduciaries like  
20 auditors who materially participate in traditional insiders'  
21 discharge of fiduciary duties because they are different from  
22 other third parties). On the other hand, under California law,  
23 this defense is theoretically available to UHY.

24       Because of this apparent material difference between  
25 Delaware and California law, and assuming both California and  
26 Delaware have an interest in having their law applied, the  
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1 Trustee contends that the court must determine which state has a  
2 paramount interest in having its law applied. *Washington Mutual*  
3 *Bank, FA v. Superior Court*, 24 Cal.4th 906, 919-20 (2001)  
4 (explaining steps involved in governmental interest analysis if  
5 one party timely invokes law of a foreign state; court is to  
6 consider each state's relative commitment to use of its laws, and  
7 consider history, current status, function and purpose of each  
8 state's laws).

9 The Trustee asserts - without elaboration or explanation -  
10 that Delaware's interests are paramount and would be more  
11 impaired if Delaware law were not applied because an aiding and  
12 abetting breach of fiduciary duty claim implicates the internal  
13 affairs of a Delaware entity and Delaware has an interest in  
14 overseeing Delaware corporate entities. The Trustee does not  
15 explain why the Debtor's operating agreement should play a  
16 central role in her claim against a non-fiduciary such as UHY.  
17 She contends only that Delaware law should be applied here  
18 despite the fact that the court previously held - at her urging -  
19 that for tort claims, California has a more significant  
20 relationship to the alleged conduct than Delaware.

21 In the Trustee's counsel's own words in referring to the  
22 fraudulent transfer claims, and her case in general:

23 [O]ur claim is not one that arises in the operating  
24 agreement. If the operating agreement did not exist, our  
25 claim for fraudulent transfer would still exist. Our claim  
26 deals with cooking the books, accounting malfeasance,  
27 creating a profit that didn't exist, and then by doing so,  
28 distributing that money. It really has nothing to do with  
the operating agreement.

1 Docket No. 165, Quadrozzi Dec., Ex. 18, transcript of 4/20/20  
2 hearing, 3:5-12.

3       The factors considered under the *Restatement (Second) of*  
4 *Conflicts of Laws* for tort claims (§145) and contract claims  
5 (§187) do not weigh in favor of using Delaware law. The Debtor  
6 was located in California, the alleged injury to the Debtor  
7 occurred in California, the conduct allegedly causing this injury  
8 occurred in California, the parties' relationship was centered in  
9 California. UHY is registered as a limited liability partnership  
10 in New York with its principal place of business in Michigan. Its  
11 audits took place in California. Many of the creditors are  
12 located in California and the Trustee acts on their behalf in  
13 pursuing the claims in this adversary proceeding.

14       Consideration of these factors does not show that the  
15 interest of Delaware is paramount to California's interest. None  
16 of the relevant events occurred in Delaware. The only connection  
17 to Delaware is that the Debtor was organized under Delaware law.  
18 The Trustee has conceded the operating agreement is tangential to  
19 her fraudulent transfer and "accounting malfeasance" claims  
20 against the Speyside Defendants and it is irrelevant to the  
21 claims against UHY as Debtor's outside auditor.

22       Based on the above authorities, the court holds that the  
23 Trustee's aiding and abetting breach of fiduciary claim against  
24 UHY does not implicate the internal affairs of the Debtor.  
25 Delaware does not have a paramount interest in having its law  
26 applied under a governmental interest analysis. In addition, the  
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1 Trustee did not timely raise this choice of law issue and the  
2 court sees no reason to allow the Trustee to depart from the  
3 position she took in her discovery responses to UHY or to depart  
4 from the position she took in response to the Speyside  
5 Defendants' motion to dismiss the fraudulent transfer claims.  
6 Aiding and abetting breach of fiduciary duty is a tort to which  
7 California law applies.

8 **C. The Unclean Hands Defense - *in Pari Delicto***

9 UHY contends that the Trustee is deemed to have been a  
10 participant in the alleged wrongdoing of the Speyside Defendants  
11 and thus has unclean hands. In other words, standing in the shoes  
12 of the Debtor, she is *in pari delicto* with the Speyside  
13 Defendants and may not recover from them and, by extension, has  
14 no viable claim against UHY.

15 California courts have applied the *in pari delicto* defense  
16 to aiding and abetting breach of fiduciary claims brought by  
17 bankruptcy trustees where the underlying misconduct can be  
18 imputed to the corporate entity and therefore to the trustee. *In*  
19 *re Mortgage Fund '08 LLC*, 527 B.R. 351, 361 (N.D. Cal. 2015)  
20 (citing cases; defense applied to liquidating trustee's aiding  
21 and abetting claim against debtor's lender; knowledge of the  
22 debtors' managers' wrongdoing was imputed to the debtor and  
23 therefore to the trustee under the sole-actor exception where the  
24 managers and the debtor were one and the same).<sup>5</sup>

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26 <sup>5</sup>Under Bankruptcy Code §541(a)(1), a trustee's rights are no  
27 greater than the rights of the debtor.

1 As noted in *In re Yellow Cab Coop., Inc.*, 602 B.R. 357, 360  
2 (Bankr. N.D. Cal. 2019), Section 3517 of the California Civil  
3 Code generally codifies the doctrine of *in pari delicto* or  
4 unclean hands: "No one can take advantage of his own wrong."  
5 Courts applying *in pari delicto* examine: (1) whether the  
6 misconduct at issue can be imputed to the corporate debtor; (2)  
7 whether the debtor's misconduct can be imputed to the bankruptcy  
8 trustee; and (3) whether the misconduct is sufficiently related  
9 to the causes of action asserted by the trustee. *Peregrine*  
10 *Funding, Inc. v. Sheppard Mullin Richter & Hampton, LLP*, 133 Cal.  
11 App. 4th 658, 679 (2005).

12 There are three steps in the analysis of whether the defense  
13 is applicable. *In re Crown Vantage*, 2003 WL 25257821, at \*7 (N.D.  
14 Cal. Sept. 25, 2003), *aff'd* 198 F. App'x 597 (9th Cir. 2006).  
15 First, the defense applies if agents of the Debtor - here the  
16 Speyside Defendants - participate in the bad acts for which the  
17 Trustee seeks damages. Second, if these agents have acted in a  
18 way that is adverse to the Debtor and instead have acted to serve  
19 their own interests, the defense will not apply (the "adverse  
20 interest exception"). Third, an exception to the adverse interest  
21 exception arises if these agents and the Debtor are really one  
22 and the same so the defense will apply (the "sole-actor  
23 exception").

24 On this record, the defense applies. The first step is  
25 satisfied because the Speyside Defendants allegedly "looted" the  
26 Debtor causing the Trustee's damages. See, for example, FAC ¶2,  
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1 8, 18, 44, 75, 77, 85, 91, 129, 166. The second step is also  
2 satisfied in that there is no allegation in the FAC - and nothing  
3 in the summary judgment record - to suggest that the adverse  
4 interest exception applies. Finally, the FAC alleges - and the  
5 undisputed summary judgment evidence shows - that the Speyside  
6 Defendants jointly controlled the Debtor, and there was, in  
7 effect, a sole actor. See FAC ¶18 ("there were no innocent  
8 insiders (officers, directors, or shareholders) of the Debtor ...  
9 who could have acted during the relevant period" and the  
10 "looting" was not discovered until after the petition date).

11 UHY has established that the alleged wrongdoing of the  
12 Speyside Defendants is imputed to the Debtor and by extension to  
13 the Trustee. The *in pari delicto* defense applies.

#### 14 **IV. Conclusion**

15 Based on the foregoing, California law applies to the  
16 Trustee's claim against UHY and the *in pari delicto* defense  
17 precludes the Trustee from recovering against UHY. The court need  
18 not reach the remaining issues raised by the parties. The court  
19 requests that UHY upload a supplemental order granting  
20 summary judgment corresponding to this ruling.

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22 \*\*\*\* End of Memorandum Decision \*\*\*  
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2 **Court Service List**

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